



A REPORT
TO THE
MONTANA
LEGISLATURE

LEGISLATIVE AUDIT
DIVISION

22P-01

PERFORMANCE AUDIT

Reinforcing Organizational Improvements in Public Service Regulation

*Public Service Commission
and Department of Public
Service Regulation*

JANUARY 2024

**LEGISLATIVE AUDIT
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REPRESENTATIVES

LYN HELLEGAARD

Lyn.Hellegaard@legmt.gov

SJ HOWELL

SJ.Howell@legmt.gov

EMMA KERR-CARPENTER

Emma.KC@legmt.gov

FIONA NAVE

Fiona.Nave@legmt.gov

JERRY SCHILLINGER

Jerry.Schillinger@legmt.gov

LAURA SMITH, VICE CHAIR

Laura.Smith@legmt.gov

SENATORS

JASON ELLSWORTH, CHAIR

Jason.Ellsworth@legmt.gov

PAT FLOWERS

Pat.Flowers@legmt.gov

CHRIS FRIEDEL

Chris.Friedel@legmt.gov

DENISE HAYMAN

Denise.Hayman@legmt.gov

KATHY KELKER

Kathy.Kelker@legmt.gov

FORREST MANDEVILLE

Forrest.Mandeville@legmt.gov

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We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Members of the performance audit staff hold degrees in disciplines appropriate to the audit process.

Performance audits are conducted at the request of the Legislative Audit Committee, which is a bicameral and bipartisan standing committee of the Montana Legislature. The committee consists of six members of the Senate and six members of the House of Representatives.

AUDIT STAFF

JULIA CONNELLEY

ALYSSA SORENSON

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Angus Maciver, Legislative Auditor
Kenneth E. Varns, Legal Counsel



Deputy Legislative Auditors:
Cindy Jorgenson
William Soller
Miki Cestnik

January 2024

The Legislative Audit Committee
of the Montana State Legislature:

We are pleased to present our performance audit of the Public Service Commission and Department of Public Service Regulation.

This report provides the Legislature information about the operations and regulatory activities of the department. This report includes recommendations for enhancing standards of conduct, internal controls, and staffing at the Department of Public Service Regulation. A written response from the Public Service Commission is included at the end of the report.

We wish to express our appreciation to Public Service Commission and Department of Public Service Regulation personnel for their cooperation and assistance during the audit.

Respectfully submitted,

/s/ Angus Maciver

Angus Maciver
Legislative Auditor

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ELECTED, APPOINTED, AND ADMINISTRATIVE OFFICIALS

Public Service Commission

James Brown, President

Jennifer Fielder, Vice President

Randy Pinocci, Commissioner

Tony O'Donnell, Commissioner

Annie Bukacek, Commissioner

Brad Johnson, Commissioner (through December 2022)

Department of Public Service Regulation

Erik Wilkerson, Executive Director (through June 2022)

Brad Tschida, Executive Director (through September 2023)

Tina Limesand, Business Manager

Lucas Hamilton, Chief Legal (effective December 2022)

Ben Reed, Chief Legal (through November 2022)

Will Rosquist, Chief Regulatory



MONTANA LEGISLATIVE AUDIT DIVISION

PERFORMANCE AUDIT

Reinforcing Organizational Improvements in Public Service Regulation

DEPARTMENT OF PUBLIC SERVICE REGULATION
A report to the Montana Legislature

BACKGROUND

The Montana Public Service Commission (PSC) regulates private, investor-owned natural gas, electric, telephone, water, and sewer companies with business in Montana. The PSC also oversees railroad and pipeline safety regulations. The Department of Public Service Regulation (DPSR) is the agency that supports the PSC through its three divisions: Legal, Centralized Services, and Regulatory.

Agency:

Department of Public
Service Regulation

Commission:

James Brown, President
Jennifer Fielder, Vice
President
Randy Pinocci
Tony O'Donnell
Annie Bukacek

Program:

N/A

Program FTE:

38

The Department of Public Service Regulation was restructured in 2021 to address past concerns of commission misconduct and management issues. The department implemented new policies and a strategic plan to improve department operations and guide commissioners, management, and staff in the department's work. We found the department has addressed many of the previous concerns and did not find evidence of improper influence on the regulatory process. However, we determined the department should further address gaps in the organizational structure and risks to the quality and effectiveness of the regulatory work, including the conduct of commissioners, the status of key positions in the department, and recruitment and retention for critical positions.

KEY FINDINGS:

Public Service Commissioners do not have a formal code of conduct to advise their behavior and activities as public officials. The commissioners have previously faced scrutiny for conduct that harms public trust in the Public Service Commission. These activities diminish the commission's reputation and complicate recruiting for the department. A formal code of conduct and regular training would help the commission assert its commitment to public trust.

The Department of Public Service Regulation has not adjusted management personnel positions within the new structure to achieve the strategic plan's goals. Though management personnel are described as reporting to the new executive director, they remain classified as personal staff of the commission. In state government, personal staff are appointed, exempt employees who serve at the commission's discretion. As such, the role of the executive director is diminished, and management staff are less able to address staff issues and concerns.

(continued on back)

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Since implementation, key positions identified in the Department's strategic plan have experienced turnover and vacancies. Without key management positions staff have experienced higher workloads and less department support to provide quality regulatory work. The Commission has struggled to fill these positions and meet the vacancy savings requirement imposed by the Montana Legislature. However, there are opportunities for the department to identify and request the necessary resources to fund these positions.

The Department has experienced high turnover in recent years which affects the quality of the regulatory work. The department has made efforts to address retention issues, including offering more opportunities for telework and flexible schedules. The department has not completely implemented retention strategies for some positions that are highly competitive or vulnerable to turnover, such as addressing disparities in pay and stagnancies in the career ladders.

RECOMMENDATIONS:

In this report, we issued the following recommendations:

To the department: 3

To the legislature: 0

RECOMMENDATION #1 (page 10):

Management and operational effectiveness

The Public Service Commission should further define a commission code of conduct and provide continuing education on the code.

Department Response: Partially Concur

RECOMMENDATION #2 (page 15):

Management and operational effectiveness

The Department of Public Service Regulation should consider and revise the appropriate classification for management level positions.

Department response: Partially Concur

RECOMMENDATION #3 (page 21):

Management and operational effectiveness

The Department of Public Service Regulation should address turnover and retention by proposing methods to the Legislature for funding the pay plan and increasing salaries for competitive positions.

Department response: Partially Concur

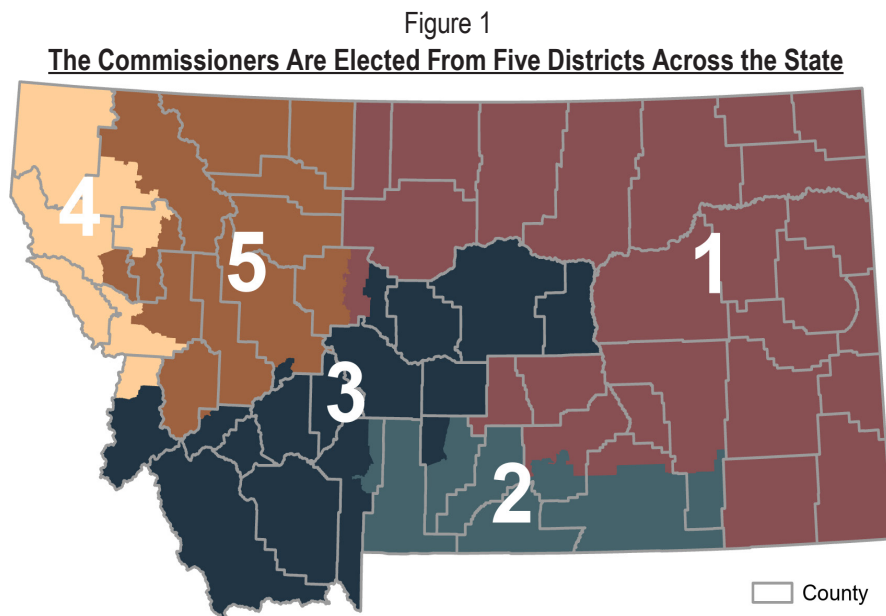
Chapter I – Introduction and Background

Introduction

The Montana Public Service Commission strives to ensure ratepayers in the state have continued access to utility services that are affordable, reliable, and sustainable, while ensuring the utility companies maintain a financially sound service. In 2020 and 2021, publicly reported upheaval and the Legislative Audit Division's Financial Compliance Audit on the Department of Public Service Regulation alerted the public to issues with the department's management controls and compliance with state laws. Subsequently, the Legislative Audit Committee prioritized a performance audit of the Public Service Commission and Department of Public Service Regulation in fiscal year 2022 to evaluate the condition of internal policies and department controls and the effects of previous concerns on the regulatory process. We conducted a performance audit to assess the Public Service Commission and Department of Public Service Regulations' management practices and organizational culture. We examined the controls in place to ensure department operations complied with internal policies, state laws, and best practices, and that the regulatory process was effective. We found the commission has designed a strategic plan and restructured the department to address many of the concerns in the 2021 financial compliance audit. We did not find evidence of improper influence on the regulatory process; however, we did find areas of improvement remain in commissioner accountability, department organizational structure, and staffing to decrease risk to the regulatory process.

History and Duties of the Public Service Commission

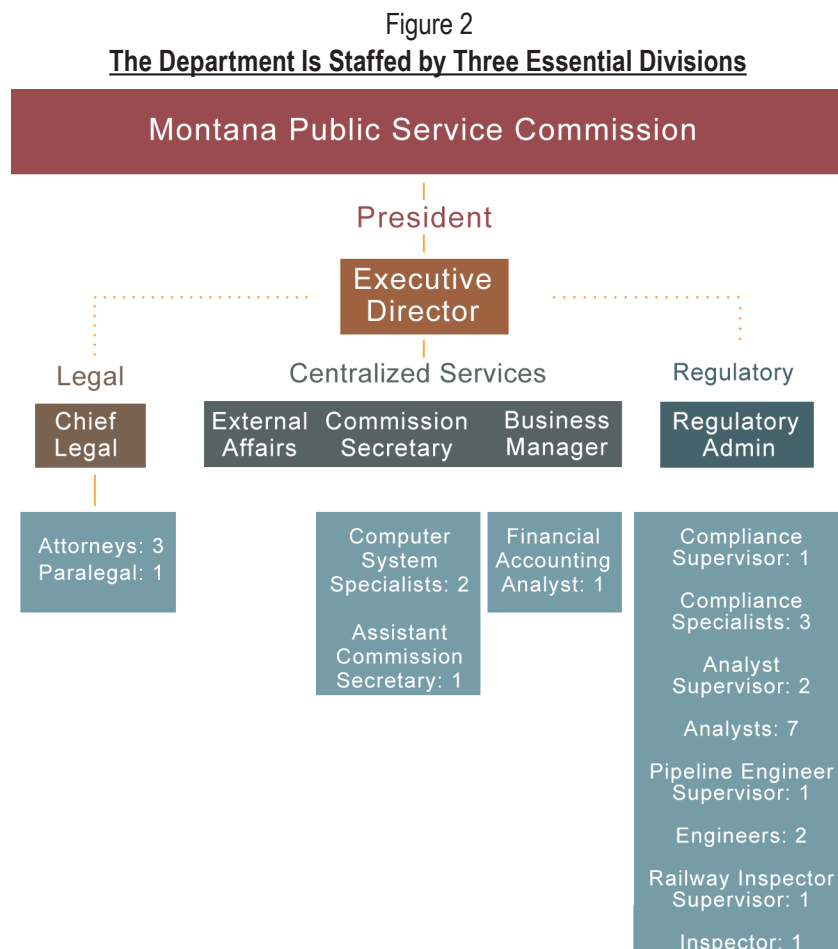
The Public Service Commission (PSC) was established in 1907 by the Montana Legislature to regulate private, investor-owned utility and service companies. The members of the PSC are elected from five regional districts to serve four-year terms. The elections are partisan, so a PSC candidate may affiliate with a political party. There are no requirements for relevant professional or educational experience or background. The members also choose one member to serve as president of the commission. The following figure shows the counties associated with each PSC district.



Source: Compiled by the Legislative Audit Division from department records.

The PSC regulates private, investor-owned natural gas, electric, telephone, water, and sewer companies with business in Montana. The PSC also oversees railroad and pipeline safety regulations and some transportation industries, such as garbage service. The mission of the PSC is to ensure ratepayers of utility companies have continued access to affordable, reliable, and sustainable utility services. This includes setting service rates and monitoring the service quality of these companies. The commission reviews rate and service filings, researches policy issues and recommendations, develops railroad safety plans, conducts pipeline inspections, assists utility customers with their inquiries and complaints, and provides timely information to the public. The PSC strives to balance the interests of consumers with those of the regulated utilities.

The Department of Public Service Regulation (DPSR) is the agency that supports the PSC. It is one of the smallest state agencies in Montana with 38 full-time equivalents (FTE) including the five commissioners. The term “PSC” is often used to refer to both the commission and the department since they work closely together. The DPSR recently underwent a reorganization of its administrative structure which now includes an executive director.



Source: Compiled by the Legislative Audit Division from department records.

Under the executive director are three divisions: Legal Services, Central Services, and Regulatory Services.

- ♦ The Legal Services Division includes a Chief Legal Counsel, staff attorneys, and a paralegal. It provides legal analysis and counsel to the commission.
- ♦ The Centralized Services Division is comprised of a business manager, the commission secretary, and an external affairs manager. In addition to those positions, the division has six FTE to provide additional administrative support, such as information technology, accounting, and public policy and media relations.
- ♦ The Regulatory Services Division is comprised of compliance specialists, analysts, engineers, and inspectors overseen by the Chief Regulator. The Regulatory Division reviews and analyzes the information related to PSC dockets and provides the commissioners recommendations for decisions. It also includes inspectors for railroads and pipelines in cooperation with federal programs.

Audit Scope & Objectives

We determined an examination of the Public Service Commission should be scoped as an examination of the PSC's organizational structure, management culture, and regulatory responsibilities of the utility and service industry. We focused our evaluation on the department's overall operations rather than specific divisions or personnel within the department. As much of the improper activities reported on by the media and the financial compliance audit occurred in fiscal years 2019 and 2020, we scoped audit work around those years and the years since to identify if the department has taken the necessary steps identified in the media and the audit recommendations to improve department operations and culture. Additionally, we were interested in assessing the organizational operations and regulatory processes to determine if the improper activities in recent years have improperly influenced the operations and processes of the department.

We developed the following objectives for examining the PSC's management practices and organizational culture:

1. Has the PSC established management controls to comply with state laws, internal policies, and best practices?
2. Does the PSC protect the integrity of the regulatory process from improper influence to promote public trust in the commission?

Audit Methodologies

To address these objectives, we completed the following methodologies:

- ♦ Solicited and analyzed staff experiences and opinions through surveys (26 staff members—a 100% response rate), interviews, and observations;
- ♦ Evaluated the department's strategic plans and steps taken to improve department's operations;
- ♦ Interviewed and reviewed other states regarding best practices for organization operations of regulatory bodies, including department structure, internal policies and procedures, and duties of commissioners and staff;

- ♦ Reviewed a sample of 9,647 emails from commissioners and management with external entities between 2019 and 2023;
- ♦ Identified and reviewed best practices for elected officials in regulatory capacities from state statute and Federal guidelines;
- ♦ Reviewed publicly available commissioner campaign information and reports, including campaign contributions and ethics complaints;
- ♦ Examined staffing issues and turnover between 2017 and 2022 to identify causes of turnover in the department; and
- ♦ Analyzed commission dockets from 2015 to 2020 to identify outcomes of the regulatory process.

Chapter II – Commissioner Conduct and Duties

Introduction

As elected officials, commissioners have a commitment to the citizens and consumers in their districts and should balance the interest of ratepayers with the need to maintain financially sound utilities capable of providing reliable service. The commission often sets service rates through contested cases where the commission takes on an adjudicatory role. The commission has a responsibility to make decisions in these cases based only on statute, precedent, and the evidentiary record, not personal bias or extraneous factors. In the past several years there have been publicly reported concerns the commission's actions may affect the regulatory process and diminish public trust in the mission of the Public Service Commission. To address the extent of these concerns, we reviewed commission docket orders and other related documents from the regulatory process, examined campaign contributions for the five commissioners, and reviewed communication between commissioners and external regulated parties. The commission and department have taken several steps to address past concerns of commissioner conduct, including revising internal policies, creating a strategic plan, and implementing an orientation process for newly elected commissioners. While we did not find instances of improper influence from the regulated industry, we did identify improvements to current practices and policies that could increase public trust in the commission and the regulatory process they oversee.

Public Officials Are Expected to Uphold Public Trust

Public officials in Montana are held to statutory requirements to uphold public trust in the integrity of public officers, legislators, and public employees. Title 2 of the Montana Code Annotated outlines standards of conduct and a code of ethics for all public officials to separate public duty from private interest. The rules of conduct outline unacceptable behavior of public officials, including the use of public funds, time, or resources for activities outside of their official duties. Ethical requirements also state that members of quasi-judicial boards, such as the Public Service Commission, who are required to take official action on a matter where a personal or private conflict exists that would give rise to an appearance of impropriety, should disclose the conflict before participating in official action.

Effective Internal Control Systems Need Commitment to Integrity and Ethical Values

The U.S. Government Accountability Office's Standards for Internal Control in the Federal Government, also known as the Green Book, sets the standard for internal controls and how they are identified, designed, implemented, and achieved. An effective internal control structure starts with the oversight body's commitment to integrity and ethical values. This includes a "tone at the top" to establish and adhere to standards of conduct. The entity's oversight body should lead by example and demonstrate the importance of integrity and ethical values through directives, attitudes, and behavior. The entity's expectations for integrity and ethical values can be communicated through internal policies, operating principles, or other guidelines.

The Effect of Commission Activities on Public Trust

Past instances of inappropriate or unprofessional behavior by commissioners have challenged public trust. The 2021 financial compliance audit of the department reported commissioners and management-level staff could exploit and override department controls. This included providing falsified documents to auditors, wasting state resources, and disregarding state and internal policies. Around this same time, the commission was in the news for issues within the department, such as concerns over bullying, harassment, and spying occurring between commissioners and staff.

Previously, commissioners have demonstrated difficulty separating campaign and political activity from their official positions. In 2020, a commissioner was fined by the Commissioner of Political Practices office for a Code of Ethics violation relating to misuse of state (PSC) property or resources in political activity. There were also instances reported in the media of Public Service Commissioners using state resources and representing the commission while making statements of their personal opinions rather than those of the commission. Two commissioners used PSC letterhead to release a statement without the support of the other commissioners warning the public of imminent energy blackouts that were disputed by the utility, which included statements favoring one source of power as a solution. When commissioners use state publication materials for individual statements rather than statements from the entire commission, this creates confusing messaging for the public and compromises public trust if messages are conflicting or unsupported. The department is revising and adopting internal policies, one of which relates to department communications. This policy should help ensure commissioner communication on behalf of the PSC is reviewed and approved prior to publication.

Communication on Regulatory Matters

As a quasi-judicial body, the commission is governed by state statute in adjudicating and investigating utility rates and services. As such, commissioners are prohibited from ex parte communication with regulated entities in open dockets. To ensure there were no improper communications with regulated entities, we reviewed a sample of commissioner and management personnel email exchanges between 2019 and 2023. The sample included all emails sent from external parties to commissioners and department management staff. We did not find any improper communication with regulated entities in the state email accounts during the sampled time frame.

Campaign Contributions and Conflict of Interest Disclosure

As elected officials, commissioners can receive campaign contributions while campaigning for the Public Service Commission. In our audit work, we reviewed campaign contributions for the commissioners in office before the 2022 election from the Campaign Electronic Reporting System through the Commissioner of Political Practices to identify contributions from regulated entities. It is not against campaign finance laws for commissioners to receive campaign contributions from individuals who work at regulated entities, and in our review, we did not see any patterns of voting behavior indicating such contributions affected commissioner votes in contested cases. In our review, two commissioners received campaign contributions from individuals who worked at entities or utilities regulated by the Public Service Commission. We identified a single instance of cumulative donations from higher-level employees at a single regulated entity. One commissioner received campaign contributions of \$1,170 from individuals at an entity regulated by the Public Service Commission. They also received an identical amount in contributions from individuals who appear to be spouses

or family members of these utility industry employees, identified as such based on last name, address, and day of donation. Commissioners are expected to self-identify potential conflicts of interest relating to substantial personal interests, such as business or other economic interests. However, there is no guidance for recusal relating to campaign contributions from individuals employed by regulated entities in Public Service Commission hearings. Nothing in Montana law requires commissioners to either disclose campaign contributions from persons employed by a regulated entity or persons who regularly appear before the commission.

While it is not common for states that elect public service commissioners to include discussions or expectations of conflicts of interest relating to campaign contributions in a code of conduct or code of ethics, one state does outline these expectations for its commissioners. The Arizona Corporation Commission, which regulates utilities along with corporations, securities, and railroad and pipeline safety, includes a section on campaign contributions and disclosure in its Code of Ethics. This section states commissioners should document contributions in compliance with campaign finance laws and includes language on avoiding any appearance of impropriety or conflict of interest and being mindful of contributions received from individuals or entities affiliated with the regulated entities. Commissioners are expected to declare any known contributions from individuals or entities affiliated with the regulated entities in aggregate of \$1,000 prior to voting on related matters. The PSC may want to consider if there is a need to outline similar expectations for consideration of disclosure prior to related contested cases.

Commission Decisions Are Important to Public Trust in the Regulatory Process

To address our objective relating to the integrity of the regulatory and public trust in the commission, we reviewed commission dockets to identify trends in commission decisions. The commission relies on the analysis of regulatory and legal staff in the department to review the facts of the dockets and make recommendations to the commission. The commission is not required to accept the staff recommendations and can decide on a final order as a commission. Contested rate cases are fundamental to the regulatory process and require strict adherence to quasi-judicial standards, as opposed to the other policy-oriented work of the commission.

Our review of 63 commission dockets between 2015 and 2020 noted that staff recommendations often anticipated a broad range of potential decisions. We found commissioners followed the staff recommendation in 97 percent of dockets. However, after the commission decisions and subsequent requests for reconsideration, five docket decisions, two of which did not follow staff recommendations, were reviewed in District Courts or the Montana Supreme Court. This included both dockets that did not follow staff recommendations. Four of these involved renewable energy productions and the courts determined the commission was biased in their decisions on these dockets and made decisions based on policy preference, rather than on the facts of the case. In media op-eds related to these cases, commissioners made statements indicating bias in their decisions on these dockets. The Montana Supreme Court used commissioner comments in the docket record to determine the commission did not make fair and unbiased decisions in these cases. Making decisions based on personal bias or facts outside of the case make the commission's decisions vulnerable to legal scrutiny and hurts public trust in the commitment to balance consumer interests with the needs of the utility industry.

Public Perception Affects the Department's Operations

In a staff survey administered in September 2022, some staff shared their concerns about the commission's reputation and, by association, the department. The news stories and visibility of the commission in recent years have affected the perception of the commission, which staff believe hurts the department. One way PSC management and staff are concerned about the effect the commission's reputation is on recruiting for the department. Some staff believe the negative coverage of the commission is a likely reason why positions are open longer with few qualified candidates.

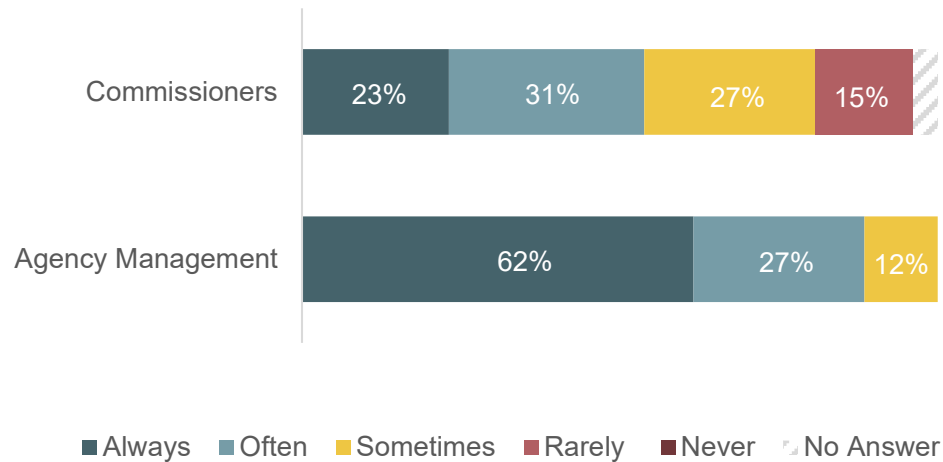
The Public Service Commission Has Partially Developed a Code of Conduct

The Montana Public Service Commission has already identified a need to further inform and educate commissioners on the duties of their role and expectations as a commission in addition to existing standards for all elected officials outlined in Title II of the Montana Code Annotated. After the 2022 elections, seeing the need to assist new commissioners in properly understanding the scope of and behaviors needed to be successful in their roles, the commission implemented a more robust orientation process for newly elected commissioners. This includes a letter detailing the position's duties, what to know, and what to expect early on. The letter speaks on some topics related to the professional conduct of commissioners, such as decisions not being made on personal biases and decisions being fair and equitable based on balancing the interests of utility companies and the interests of customers. However, the letter does not include further expectations of conduct for balancing duties as an elected official versus duties as a regulator, such as campaigning for reelection independently from commission duties. This guidance is only provided during onboarding, so only one commissioner has completed the new orientation process. The additional orientation materials and improved orientation process are part of what the department considers a more comprehensive approach to address past issues, including revising internal policies and restructuring the department.

Feedback from the staff survey identified the need for additional commitment to self-accountability by commissioners in the ethical values they exhibit. In the survey response, about 60 percent of staff believe management always exhibit high ethical values, while only 23 percent of staff believe the same for commissioners. Staff believe the commissioners generally set the tone for the agency, and their elected, political positions create some difficulty for staff. Being elected officials also makes it hard for staff to believe commissioners are held accountable for their actions – only 50 percent of staff agree commissioners are held accountable for inappropriate behavior. Self-regulation and education are important because commissioners are elected officials.

Figure 3
Department Staff Believe Management Exhibits High Ethical Values More Often Than Commissioners

How often do commissioners and agency management exhibit high ethical values?



Source: Compiled by the Legislative Audit Division from PSC staff survey responses.

With a code of conduct specific to the Public Service Commission, the PSC can clarify and extend how the department's mission and goals of the department are articulated through the commissioner's professional conduct. Written codes of conduct can be a central guide for commissioners and staff and help measure organizational performance, including bolstering staff perception and confidence in commissioner actions. Codes of conduct also help build a positive culture and reassure staff and the public of the commission's commitment to integrity and ethical values. We believe a code of conduct would reinforce the steps the commission has taken to address the expectations and conduct of commissioners.

Rules of Conduct in Other States

As part of our audit work, we identified other state service and utility commissions with codes of conduct for commissioners. The California Public Utility Commission has a commissioner code of conduct outlining commissioners' duty to conduct themselves with integrity and act in the public interest. The rules are intended to ensure due process and fairness for all interested parties and the public. This includes being clear when commissioners are acting professionally or representing personal interests, serving as a model of leadership, integrity, and civility to the public in every action and statement, and ensuring commission activities and orders are fair, unbiased, and reflect the positions of all commissioners. The Pennsylvania Public Utility Commission also has a code of ethics specific to the commission in state statute. This code includes avoiding impropriety and the appearance of, performing duties impartially and diligently, abstaining from publicly expressing personal views, disqualifying from official proceedings in which impartiality may be questioned, and regulating extra-curricular activities to minimize risk of conflict with official commission duties, among others. Our review work

of other states indicated that it is important for commissioners to delineate between the judicial-style commission duties, like docket proceedings, and the political-style duties as elected officials, like campaigning and speaking to constituents on personal policy preferences. Commissioners should also be regularly educated on the expectations of their duties.

RECOMMENDATION #1

We recommend the Public Service Commission:

- A. *Expand and further define a commissioner code of conduct to assert commitment to public trust.*
 - B. *Establish periodic continuing education for commissioners and staff on the code to ensure the standards and expectations are understood and followed.*
-

Chapter III – Key Management Positions

Introduction

From 2021 Financial Compliance Audit results, the Department of Public Service Regulation was tasked with creating a strategic plan, which included a reorganization of the department structure, and ensuring internal policies and state laws were followed. To address whether the department has established management controls, we reviewed internal policies and the strategic plan, surveyed and interviewed department staff and management, conducted observations, and identified best practices for management controls. While it is clear the department has made improvements in updating and formalizing internal policies and defining a chain of command and expectations for key positions in the new organizational structure, there are areas the department should further address to strengthen their ongoing organizational efforts and ensure previous instances of misconduct do not happen again.

Organizational Structures Need Defined Responsibilities and Delegations of Authority

As part of our work, we identified best practices for organizational structures and how other state service and utility commissions have structured their commissions and supporting departments. A successful organizational structure is key to ensuring the internal controls within an agency are effective. The U.S. Government Accountability Office's Standards for Internal Control in the Federal Government, also known as the Green Book, sets the standards for internal controls and how they are identified, designed, implemented, and achieved. The organization structure, responsibilities, and delegation of duties are necessary for establishing an effective internal control system. The structure and responsibilities allow the organization to operate efficiently. The oversight body and management need to assign and delegate authority so that key roles properly segregate duties to prevent fraud, waste, and abuse within the department. Additionally, best practices state that authority should increase as positions move up the organizational structure, so those at the top have more formal authority than those below.

Other State Commissions Have Established an Executive Director to Head the Supporting Department

Many state agencies and organizations often include an Executive Director as the head of the department, rather than the oversight body such as a board of commission. This is also a common practice in the public service or utility commissions in other states, as well as being good management practice. States nationwide vary in commission membership, as the state's governor or legislature appoints many commission positions, and 11 states, including Montana, elect their commissioners. Three states we reviewed more closely in audit work included Minnesota, Utah, and South Dakota. Minnesota has a five-member commission appointed by the governor, while Utah has a three-member commission appointed by the governor. Like Montana, South Dakota is one of the few states that elect commissioners. South Dakota has a three-member commission.

The Department's Restructure of Upper Management Positions Is Not Fully Effective

The department's restructuring to include an executive director and other management level staff was part of an effort to address previous instances of commissioners and staff overriding or ignoring department controls. During the 2021 financial compliance audit of the department, commissioners and management-level staff could exploit the organizational structure to override department controls. Auditors were concerned about the integrity and competence of certain management personnel, which auditors believed resulted in a poor department culture. As a result, the audit recommended the department implement a plan to improve department culture and develop, implement, and monitor internal controls to comply with state and internal policies.

The Strategic Plan Identified Key Positions to Address Previous Gaps in Management Structure

The commission and department developed a strategic plan to improve department operations, performance, culture, and reputation of the commission and department. The plan's first goal was to improve the organizational structure by defining leadership roles and responsibilities and establishing a chain of command. The department established an executive director position to serve as the chief administrative officer of the department and the administrator of the Centralized Services Division. The new chain of command and reporting hierarchy described in administrative rule places the Executive Director above the other management-level positions in the organizational structure.

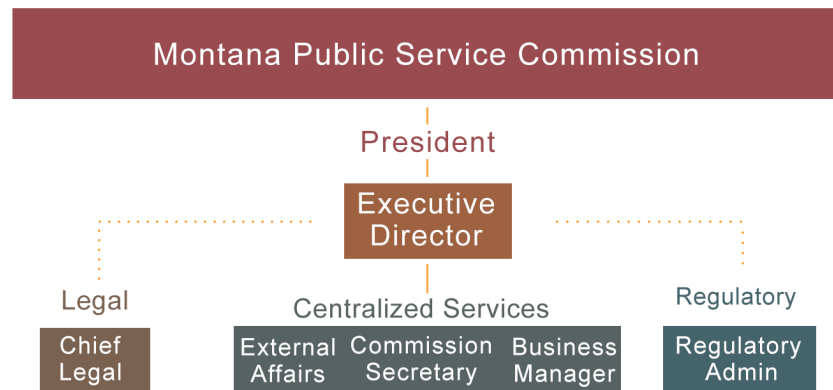
The commission and department developed a strategic plan to improve department operations, performance, culture, and reputation of the commission and department.

However, the new organizational structure did not adjust the authority of the Executive Director or the other management-level positions, as appointed positions, to delineate any additional authority this position may have relative to the others. As a result, while the division administrators review the performance of staff within their division, the Commission, rather than the Executive Director, reviews the performance of all appointed staff including those within the Centralized Services Division. The Executive Director is tasked with monitoring the performance of the agency without formal tools or authority to do so. Recently commissioners have described a vision for the position to serve in an advisory rather than a management role to the other management level positions, and as such do not feel it requires additional authority over department staff and operations. This inconsistency has created ambiguous lines of authority within the organizational structure and threatens the effectiveness of the position.

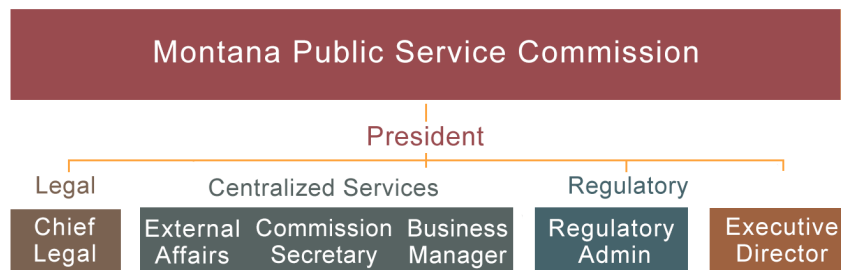
Figure 4

The New Organizational Structure Creates Ambiguous Lines of Authority Between Commissioners, the Executive Director, and Management

The first chart shows the department's organizational structure as defined in administrative rule.



The second chart shows the organizational structure as it functions with no additional authority given to the Executive Director relative to the other management positions.



Source: Compiled by the Legislative Audit Division from department records and LAD analysis.

Staff Are Concerned About the Effectiveness of the New Structure

In the staff survey and interviews, we spoke to staff about the department organization and operations. Overall staff reported improvements in the chain of command with the addition of an executive director. However, staff were concerned about management staff continuing to serve at the pleasure of the commission and how that might affect management's ability to address inappropriate behavior in the department. Staff expressed interest or hope that management level staff would change to nonexempt positions rather than personal staff positions so that management can better address staff issues and staff can feel more comfortable reporting improper behavior. It is difficult for staff to feel confident in management's ability to address issues with commissioners because those appointed

positions do not provide job security. An inability to address issues and concerns affects staff morale and the effectiveness of department operations. A few staff members reported to us that they had personally experienced unprofessional behavior but did not report the incident because they assumed management would not address it, or they would face consequences for reporting.

The Status of Management Positions Does Not Allow Management to Address Staff Issues and Enforce Compliance With Internal Policies

Management positions in the department, including the executive director, the business manager, the commission secretary, the external affairs manager, and the chief regulator, are classified as exempt, personal staff. State law allows no more than six personal staff positions to the PSC and the commission has chosen to allocate five of these positions to the management staff with key operational responsibilities. Traditionally in public service these positions are used in top leadership or policy-oriented positions. The chief legal is the only management position that is classified as a nonexempt employee. According to the State Human Resources Division, personal staff serve at the discretion of the elected official. They are entitled to employee benefits only as extended by the statute or by agreement with the elected official. This means the individuals serving in these positions do not need to be hired through a competitive process and are excluded from many common Montana Operations Manual policies and nonexempt state employee protections. The commission appoints each of these key positions. The PSC currently is allowed six personal staff positions with five in use, but only three filled.

The Commission Has Previously Considered Reclassification

In 2020, the department was sued by a former Chief Legal Counsel for wrongful termination and violation of due process rights. The Chief Legal Counsel, who was classified as exempt at the time, alleged the commission asked them to resign for expressing concerns over human resource issues in the department and refusing to expose employees who had complained about harassment in the department. When the Chief Legal did not resign, the commission voted to terminate them. The department later settled the lawsuit with the former chief legal, however, the department did not admit any liability.

In recent years, the commission has reportedly had discussions with certain management-level staff as to whether reclassification to nonexempt status is reasonable for those positions. The commission recently reclassified the chief legal position to nonexempt status. As the commission has considered the need for certain management positions to be classified as nonexempt, the classification status other management staff responsible for key department operations should be carefully considered.

Other States Appoint Executive Directors as Head of the Department

We were interested in the department structure and delegation of authority in other state commissions to identify best practices for Montana's restructuring. States like Minnesota and South Dakota employ an Executive Director or Secretary as head of the department that supports the Public Utility Commissions in those states. These positions are appointed by the commissions and manage the department operations. In Minnesota, the Assistant Executive Secretary and the General Counsel are also appointed by the Minnesota Public Utilities Commission; however, the other management level staff are hired by the Executive Secretary.

RECOMMENDATION #2

We recommend the Public Service Commission revise the appropriate classification for management level positions to formalize and complete the department's organizational structure.

Turnover in Key Positions Threatens New Management Structure and Controls in Place

The PSC's organizational structure highlights the key pieces in management and department operations. The Executive Director acts as the department manager and chief of staff. That position should oversee management staff and the Centralized Services Division. They should also oversee internal policies and procedures, audit compliance, staff workload, and department performance. The Executive Director should act as the top of the chain of command for the department and mediates between the commissioners and department staff. Department management includes the Chief Legal, Business Manager, Commission Secretary, External Affairs Coordinator, and Chief Regulator. These positions are key in establishing and performing the reporting structure within the department. Management oversees and coordinates all department-level duties in their respective areas. Leadership should ensure the department fulfills its mission and complies with state laws, internal policies, and best practices.

While there is a recognition of the importance of the role of these staff, many of the key positions identified in the PSC's strategic plan and new organizational structure have experienced turnover and vacancies since 2021. The department lost two executive directors, a chief legal counsel, and an external affairs coordinator. Since 2017, the department lost seven personal staff members. The department hired and lost two executive directors since August 2021, with a six-month vacancy between the two and the position currently open. Similarly, the external affairs coordinator was hired in early 2021, and the position has been vacant since mid-2022. When these positions are vacant, no interim staff is appointed to fill the duties, though some of the executive director responsibilities go to the President of the Commission.

The executive director position was intended to provide a buffer between commissioners and department staff by managing staff operations and advising the commission on internal matters. However, since its implementation, the executive director position has experienced turnover and long-term vacancy. Seeing major hires leave has burdened the remaining staff with duties and has created additional stress on staff. Throughout audit work, staff expressed optimism toward the executive director position. Still, it is unclear what kind of impact the position would have on department operations without having someone in that position long-term.

The Department Should Ensure Key Positions Are Filled

Vacancies in key positions within the department's organizational structure have persisted in recent years. Early on, the commission reported that constraints on the department's personal services budget were the reason for a "hiring freeze" for the Executive Director and External Affairs Manager position

after increasing pay to be competitive in other key positions, such as a certified public accountant in the Centralized Services Division. Commissioners spoke of the importance of hiring and filling these positions, especially the Executive Director, to help balance workloads among staff and provide effective communication between commissioners and staff. The hiring freeze was also intended to ensure the department met the agency vacancy savings requirements imposed by the Montana Legislature. The Legislature imposed a five percent vacancy savings requirement on the commission during the 2023 Legislative Session. The PSC is one of the smallest agencies, and the vacancy savings requirement is reportedly a larger burden to meet than larger agencies. However, the department's strategic plan and administrative rule identify these positions as critical to the department's operations. As such, it is important for the department to identify and request the resources necessary to fund these positions.

CONCLUSION

An Executive Director, and other management level positions, are key positions in the success of the department's operations. It is important the department prioritize hiring and filling these positions for long-term success of the organization.

Chapter IV – Staffing for Quality Regulation

Introduction

The Department of Public Service Regulation supports the Public Service Commission through regulatory reviews and analyses, legal counsel, consumer assistance, pipeline and railway inspections, and other duties. Department staff are integral to the regulatory process from the information and analyses they provide to the commission. However, the department has experienced high turnover and difficulties recruiting in recent years. There are concerns regarding the level of turnover and the potential to diminish the efficiency and effectiveness of department operations.

To identify why turnover occurs in the department, we reviewed recruitment policies and initiatives, analyzed turnover data, compared department salaries with those in the private sector, reviewed exit interviews, and spoke to staff regarding their perception of turnover.

Commitment to Recruitment and Development of Staff Is Important

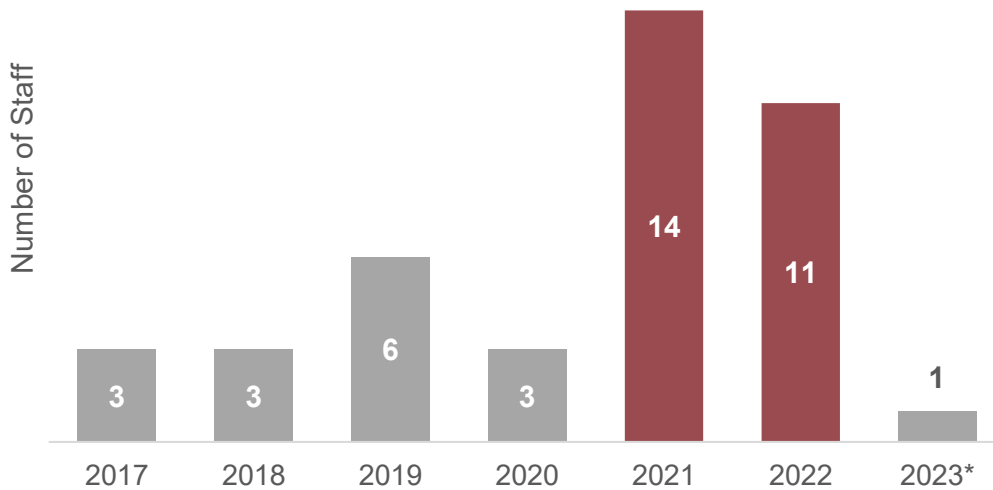
Competent staff in an organization is key to ensuring internal controls are effective. According to best practices, an organization's management should demonstrate a commitment to recruiting, developing, and retaining competent staff. This is done through defining expectations of competence; recruiting, developing, and retaining staff; and preparing succession and contingency plans. Management should recruit individuals that fit the needs and competencies of the organization and allow staff to develop competencies through training and mentorship. The utility industry is full of complex and technical issues that commissioners, analysts, attorneys, and other staff need to understand well to perform quality regulatory duties. Other states, like South Dakota, reported being successful in recruiting experienced staff from the utility industry and have retained staff by focusing on salaries for especially competitive and vulnerable positions.

High Turnover Impacts Quality and Effectiveness of Department Work

In our audit work, we analyzed turnover data for permanent staff for the Department of Public Service Regulation from 2017 to 2023 to assess turnover trends and the effects turnover has on the regulatory process. Our turnover data included turnover rates, reasons for leaving, and position type. The department experienced high turnover levels in 2021 and 2022. Previously, the department had a stable turnover rate of about between 2017 and 2020. The department is moving back toward that rate in 2023 with the help of retention strategies like telework opportunities and flexible scheduling.

Figure 5
Turnover Rates Spiked in Recent Years

Staff turnover remained consistent from 2017 to 2020 before a **two-year spike in 2021 and 2022**.



Source: Compiled by the Legislative Audit Division from September 2023 SABHRS export.

*Through September 2023.

The department saw the most turnover with personal staff and utility rate analysts during this time frame, with seven staff in each position leaving. We heard during assessment work that staff often move to the utility companies for higher pay, leave for other opportunities, or leave due to management issues. From the data we reviewed, we determined the main reason listed for staff leaving was a career choice. We could also determine the high turnover in utility rate analysts were for a career choice, more pay, and retirement. This position is highly technical and requires high levels of expertise. Losing staff in these positions can diminish the department's institutional knowledge of the regulatory process.

Exit Interviews and Staff Survey Detail Reasons for High Turnover

We reviewed exit interviews conducted by the department in 2022 to help identify why staff left the department. While staff reported enjoying spending time with coworkers and the organizational environment, many were frustrated with the duties of their jobs, such as those outside their job descriptions. These staff mainly spoke of receiving other job opportunities unavailable at the department, including more flexibility in schedules.

In addition to reviewing exit interviews, we included turnover-related questions in our survey of department staff. In the survey, 50 percent of staff reported looking for other job opportunities in the past due to wanting a better work-life balance, more opportunities for career advancement, more flexible schedules, higher pay, and not feeling their work contributes to the PSC's decisions. These areas were reflected in the interviews we conducted with staff as well.

Staff Are Concerned About the Effect of Turnover on Workloads

High turnover in the department can lead to higher workloads, low staff morale, and difficulties recruiting competent staff, threatening the quality of the regulatory work. In our interviews and survey responses, staff believe they can work effectively even with heavy workloads; however, this is still a risk to the quality of the work. Many staff were concerned that turnover and vacancies in the department, especially among experienced staff, contribute to their heavy workloads. According to staff, turnover is the most consistent issue related to their workloads. They believe turnover affects individuals and the department because the divisions lose critical knowledge when staff leave. The department has lost six veteran staff to retirement since 2017, and the high turnover among other staff, such as utility rate analysts, is concerning to staff because the department will not have the knowledge, skills, and abilities required for quality regulatory work. Staff believes retention is even more crucial as the commission's work is highly technical and complex. It would benefit the department to hire staff with previous industry experience to aid organizational knowledge. However, staff believe that is difficult without more competitive pay.

Additionally, staff reported that the department's regulatory and policy work tends to be more reactive than proactive with the high turnover and vacancies. This is because staff who stay with the department tend to take on the duties of those who leave and are too overworked to participate in proactive duties, like regional analysis and resource adequacy. This also could diminish the effectiveness and quality of the department's work when staff are not able to balance and maintain key duties.

Turnover Further Diminishes Staff Morale and Department Culture

While improving, the recent high turnover in the department will likely continue to affect staff morale and the quality of the regulatory process without commissioners and management addressing why turnover occurs. The staff survey identified 15 percent of staff who are dissatisfied with their jobs, as they do not feel they are recognized for their work, their workloads are too high, they don't like the workplace culture, the pay is too low, and there are too few opportunities for advancement. Previously, auditors identified a poor organizational culture in the department. According to our staff survey, 26 percent of staff are dissatisfied with the current culture within the department. Low morale can then catalyze even more turnover in the department.

Insufficient Pay and Ineffective Career Ladder Leads to Turnover

The main themes and issues we identified in department operations were staffing and retention. While the department has taken steps to address additional benefits like telework opportunities and more flexibility in staff schedules, they still need to address disparities in pay and stagnancies within the career ladders. Several staff, especially those in the regulatory and legal divisions, believe they have high workloads because of the type of work and the turnover in those departments. Staff often felt the divisions had to be reactive rather than proactive in their approach to the work. Staff believe pay is a major factor in retention and turnover, believing pay is not competitive, pay bands are not clearly communicated, and career ladders are not implemented or acted on. Staff believe management and commissioners have focused on the hiring needs identified in the strategic plan (like hiring an executive director) without giving enough attention given to current staffing issues in the regulatory and legal divisions.

Some department positions, like those in the regulatory and legal divisions, would benefit from candidates with prior industry knowledge. However, staff believe hiring experienced candidates would be hard without pay that is competitive enough with the utility industry or similar Federal positions. We compared salaries for three positions in the department with equivalent positions in the Montana utility industry. While pay bands in the utility industry were wider, salaries were comparable for regulatory analysts and compliance specialists. However, the maximum attorney salary in the department was only \$2,500 more than the minimum starting salary in the industry.

Table 1

Maximum Salary for PSC Attorneys Is Comparable to Starting Salaries in Utility Industry

Pay Range	Public Service Commission		Private Energy	
	Minimum	Maximum	Minimum	Maximum
Attorney	\$81,000	\$95,000	\$92,500	\$151,400
Accounting Analyst	\$63,520	\$79,400	\$50,200	\$113,400
Compliance Specialist	\$45,000	\$50,000	\$38,334	\$58,998

Source: Compiled by the Legislative Audit Division from department and industry records.

During audit work, staff questioned the lack of upward movement in the department. Staff who had been at the department for some time felt they were currently stuck in their positions. With such a small agency, staff felt there weren't many opportunities for progress. One issue staff claimed they faced moving up the career ladder is budget. Staff felt they were being held back from moving to higher positions because the budget would not allow for the higher salaries that came with promotions. Staff said the department has lost a lot of staff because there is little room to grow. However, many staff are doing the work of more senior positions while still being paid at the lower career ladder positions. Staff also worried about their progression once more veteran staff leave. They fear losing too much institutional knowledge, especially in the regulatory division, and their own growth will be limited. The department has tried to address issues in recruitment and retention but has not been able to fully implement strategies to improve turnover. This will continue to create retention issues as new staff hired in the past two years gain experience but cannot move up the career ladder.

Budget limitations were the key reason staff identified why they were being held back from competitive pay and advancement opportunities that matched their responsibilities. Commissioners say the department has not been historically successful requesting appropriations from the Legislature that would help fund the necessary positions and career ladders. However, commissioners also describe strategically curtailing their budget requests the last two sessions while working on repairing the department's reputation with legislators. As a result, they have not felt able to request the full amount necessary to meet their budgetary needs. The department requested and was partially granted additional FTE during the 2023 Legislative Session but did not request other personal services increases. The department has reported raising salaries for attorney positions to become more competitive with the private industry and other state attorney positions. However, the department has not increased its budget to fund existing staff-level position career ladders.

RECOMMENDATION #3

We recommend the Public Service Commission and Department of Public Service Regulation address turnover and retention by proposing methods to the Legislature for funding the pay plan and increasing salaries for competitive positions.

PUBLIC SERVICE
COMMISSION

COMMISSION RESPONSE

Montana Public Service Commission



James Brown, President
Jennifer Fielder, Vice President
Tony O'Donnell, Commissioner
Randall Pinocci, Commissioner
Dr. Annie Bukacek, Commissioner

January 12, 2024

Mr. Angus Maciver
Legislative Auditor
State Capitol Building
Room 160
PO Box 201705
Helena, MT 59620-1705

RECEIVED
JAN 12 2024
LEGISLATIVE AUDIT DIV.

Dear Mr. Maciver:

The following constitutes the written response of the Department of Public Service Regulation, also referred to herein as the Montana Public Service Commission (PSC) or the "agency," to the Performance Audit entitled "Reinforcing Organizational Improvements in Public Service Regulation," dated January 2024.

OVERVIEW:

The PSC appreciates that, after a lengthy, exhaustive, two-year review, the Legislative Audit Division expressly recognizes the significant improvements to agency operations and culture made by the PSC since January 2021. In particular, the PSC appreciates the Audit's notation that it "found the department has addressed many of the previous concerns" relating to agency management.

In January of 2021, incoming Commission leadership began a comprehensive process of redressing the management deficiencies occurring during the 2019-2020 time period. In the three years that have passed, the Commission has:

- (1) extensively restructured the agency and its organizational rule to better define the agency's chain of command and operations;
- (2) undertaken a complete overhaul and rewrite of the PSC's internal operations policies and manuals, including those policies that govern the Commissioner conduct;
- (3) parted ways with underperforming senior staff; and
- (4) hired experienced senior staff in the agency's Centralized Services Division.

These reforms resulted in the PSC receiving a clean fiscal Audit for the first time since the fiscal period ending June 30th, 2014. It also resulted in passing other Audits, including obtaining a perfect score on the

Commission's federal pipeline Audit. These successful results were obtained concurrently with the Department effectively handling one of its highest regulatory workload cycles starting in late 2022 and running through the entire 2023 year.

The concerted effort by the current Commission to strengthen the agency's internal operations has likewise been done in conjunction with other efforts to improve the performance of the agency. Such efforts include instituting evaluation criteria and metrics for determining staff and agency performance and creating an Executive Director position to assist with the day-to-day operations and help fulfill agency strategic planning objectives. Further, to redress staff workload issues, the agency has sought assistance from the Legislature in restoring FTE levels to traditional levels after the Legislature made personnel cuts of 3.5 FTE during the 2017 Legislative Session and by seeking legislative authority to fund the three additional FTE for the State's railroad safety program as the same was recommended by the Legislative Audit Division almost a decade ago.

Findings in the current Audit related to staff workload concerns can be attributed, in large part, to current staff having to cover the job duties of those FTE positions that were eliminated by prior legislatures. The reality is that, as a result of prior FTE cuts, the Department has had to carry out its regulatory obligations with less staff, making such adjustments in workload as have been necessary in order to satisfy the statutory demands of the agency. Such stopgap measures include work weeks exceeding 40 hours, employees forfeiting their duly earned vacation time, bringing in temporary employees during critical peak workload periods, and having Commissioners themselves undertake certain management-related responsibilities.

The agency's extensive reforms are given only cursory recognition in the Audit report and are, disappointingly, not highlighted or discussed in detail. During the Audit process, the Commission requested the Audit report properly cover the scope and breadth of these reforms. However, the Auditor declined that request. As such, these efforts are highlighted here.

In addition, as discussed below, the Auditor denied the Commission's request that the Legislature be added to two findings in this Audit. To wit, as has been communicated by current PSC leadership to the Legislature on multiple occasions, the Legislature must act as a partner to the agency if the Commission is to satisfy Audit recommendations to the agency numbered two (2) and (3).

Specifically, the Legislature must end its continued imposition of a vacancy savings requirement upon the PSC if it desires to have the agency satisfy Audit recommendations regarding filling the entirety of its upper management positions. The current vacancy savings requirement, totaling over \$336,000 this biennium, forces the agency to keep open one senior management position in order to meet the legislature's vacancy savings mandate. Therefore, the agency is being placed in an untenable position in regard to meeting its staffing needs. It is grossly unfair to fault, as this performance Audit appears to do, the PSC for meeting its legislatively imposed vacancy savings obligations.

What is more, the legislative Auditor placing the onus on the PSC to lobby the legislature to fully fund positions at 2002 market rates of the State Pay Plan puts the agency in a difficult position. After all, it is the legislature's constitutionally based purview to fund the Pay Plan. If the legislative Auditor recommends that the PSC pay its staff at market rates, then it must also recommend that the Legislature fund the PSC's personnel budget at market rates.

The Commission is also disappointed that the Audit does not contain a separate, distinct key finding that the Auditors found no evidence of improper influence or "regulatory capture." For years, there have been unfounded assertions by members of the public that the Commission's decision-making process was being improperly or unlawfully driven by regulated parties. In fact, according to the Audit

Committee's own records, the original request for this performance Audit was based on an assertion that the public was questioning if the "PSC is capable of its mission."

The single most important takeaway from the Auditor's two-plus years of audit work relates to the finding as to the soundness and integrity of the Commission's regulatory work and processes. Again, the Commission requested that the Auditors include this observation as a standalone finding. The Auditors declined to make this request as well.

The Commission is concerned that the usefulness of the Audit findings is undermined by the extreme length of time it has taken for this audit to be completed. This Committee authorized the agency's performance Audit at its October 2021 meeting. Information obtained from staff surveys and interviews used by the Audit Division to support the Auditor's findings is now two years old, resulting in stale information. To address this staleness concern, the Commission recommended that it would be both beneficial to the agency and to the members of the Audit committee to have the Auditors resurvey and reinterview staff in the fall of 2023. A second survey would be a verifiable measure to determine whether agency personnel believe current management's extensive operational reforms taken since January of 2021 are working. Again, this agency request was rebuffed by Audit staff.

Finally, the Department is disappointed that the Audit Report does not clearly delineate that the prior issues that harmed the agency's reputation and undermined public trust occurred prior to the Committee authorizing the present performance Audit. This Report would have been improved by recognizing that the Audit found no evidence that any current Commissioner or senior management staff is engaging in unethical or unlawful conduct, and that past internal strife has no bearing on the agency's important regulatory work.

Even so, the Commission appreciates the Audit Division's identification and discussion of areas where the Commission can further build upon the extensive improvements the agency has already made. The Audit findings and report reinforce areas of improvement the Commission has itself previously identified. For example, the Commission was already in the process of revising its internal code of conduct as of the Audit release date. Further, as noted in the Audit Report, the Commission has been engaged in a three-year long budgeting process designed to address employee turnover and retention issues, which included a now-completed effort to shore up the agency's centralized services and legal divisions. Prior to 2021, pay in these two divisions was grossly uncompetitive both as compared to pay in the private sector and as to other state agencies. Further, as noted in the report, the agency has instituted work schedules that allow for flexibility and work-from-home options. And, the agency has instituted a yearly performance and agency culture review, which consists of management assessing areas of agency risk and finding solutions to mitigate the same.

BACKGROUND:

In October of 2021, the Legislative Audit Committee voted to have the Audit Division conduct a performance audit on the agency. As denoted on the Committee's website, the Audit was the result of a committee member's request to have the Legislative Auditor analyze the PSC's organizational focus on essential duties, including rate setting, validation, and energy investments. See, letter of Senator Christopher Pope dated April 20, 2021.

On May 11, 2022, the committee held an Audit entrance conference. The Audit Division reported that it started its fieldwork in April of 2022. Similar to that request for review made by Senator Pope, one of the identified Audit objectives was to determine if the Commission protects the integrity of the regulatory process from improper influence to promote public trust in the Commission.

At that time, the Legislative Audit Division represented that its fieldwork would be completed by November of 2022. And, in turn, the LAD stated the draft Audit report was to be given to the agency by February of 2023.

Staff surveys were conducted from September 7th through 16th, 2022. The agency was provided with initial findings in October of 2023. The final report was given to the agency on December 19, 2023 – a few days before Christmas.

AGENCY RESPONSE TO THE RECOMMENDATIONS

A. The Agency's own recommendations.

As noted, the Commission maintains that several aspects of the report need to be supplemented and/or revised.

First, the key findings should be amended to include the following finding:

“The Department of Public Service Regulation is meeting its statutory duties and mission. After an extensive and thorough two-year review of agency operations and process, the Department is satisfying its statutory duties and doing so in an impartial manner. There is no evidence of regulatory capture or improper influence on the regulatory process. And there is no evidence that the prior issues occurring among agency management during the 2019 and 2020 time periods negatively impacted the agency's essential operations, namely rate setting, validation, and energy investments.

Second, the recommendations section should be amended to read as follows:

RECOMMENDATIONS:

“In this report, we issued the following recommendations:

To the department: 3

To the legislature: 2

Recommendation #1 to the Legislature:

Management and operational effectiveness.

The Legislature's application of the 5% vacancy savings requirement, despite Commission requests for such exemption, results in the Commission having to keep at least one key management position unfilled at all times. As noted in the report, vacancies in key management positions undermine the Department's recently implemented strategic plan and shift workload responsibilities to other Commission staff, thereby harming personnel retention efforts. Further, prior legislative reductions to PSC FTE levels have created difficulty for the agency in terms of engaging in meaningful succession planning and adequate training time for new hires.

Recommendation #2 to the Legislature.

Management and operational effectiveness.

The PSC is not an enterprise agency. Therefore, the PSC operates within budget and appropriation levels and constraints designated by the Legislature. The PSC has no authority to either unilaterally increase its appropriation authority to fund the State's pay plan or to increase position funding for competitive positions. What is more, the Agency is not authorized to implement agency-wide raises. Therefore, in

order to ensure the PSC satisfies Audit Recommendation #3, the Legislature must approve, during the 2025 Montana legislative session, the Department's proposed methods to allow the agency to fully fund the pay plan and to increase budgets for competitive agency positions.

B. Agency response to the three existing recommendations:

RECOMMENDATION #1

Department Response: Partially Concur

RECOMMENDATION #2

Department Response: Partially Concur

RECOMMENDATION #3

Department Response: Conditionally Concur

RECOMMENDATION #1 (page 10):

Management and operational effectiveness.

The Public Service Commission should further define a Commission code of conduct and provide continuing education on the code.

Department Response: Partially Concur.

As noted by the Legislative Audit Division, there is no existing statute or state policy requiring the Department of Public Service Commission to promulgate a code of conduct that is different than that already set forth in Montana Code Annotated Section 2-2-121, Rules of Conduct for Public Officers and Public Employees.

However, the Department has, on its own initiative, adopted agency-specific rules of conduct. The Department's operations manual, internally referred to as the "blue book" presently discusses and details the agency's own conduct code. The blue book details that Commissioners are to be aware of and follow Montana's statutory standards of conduct for elected officials, including Montana's statutory code of ethics. See, Title 2 MCA. The blue book also sets forth six additional ethical standards, ranging from a prohibition on ex parte communications to an obligation to report illegal or unethical behavior on the part of an employee or a Commissioner. The Committee and public should be aware that the agency's internal operating manual was in place during the turbulent 2019-2020 time period, including that portion of the agency's own ethics policy which requires Commissioners to conduct themselves in "accordance with the law in a manner that promotes public confidence in the integrity of the Commission."

Even so, since 2021, the Commission has affirmatively addressed both staff and Commissioner conduct in a comprehensive manner that far exceeds what a single Code of Conduct document could achieve. Specifically, the Commission has:

- a) developed an agency Strategic Plan which sets forth a roadmap for transforming the agency into a model of good governance;
- b) completed comprehensive revisions to the agency's Organizational Rule (ARM 38.1.10), which better define organizational areas of operation, duties, and authorities; and

c) commenced a full and complete revision of the agency's internal operations policies, namely the blue book, which has resulted in the adoption of 22 new internal policies to date and 6 additional policies in progress.

These internal policies range from outlining the agency travel approval process, to defining acceptable employee conduct at the workplace, to working through Commission leadership before engaging in communications with the media. All the aforementioned efforts have worked in concert to establish widespread, significant, and necessary guidance for Commissioners and staff regarding every aspect of agency operations.

The recommendation to further define a code of conduct and provide continuing education is well taken and entirely consistent with the direction the PSC has taken and is currently taking. In addition to adhering to the State's statutory code of ethics, the agency is in the final stages of implementing a revised internal conduct code. This effort is being carried out in conjunction with and in conformance with the goals and objectives set forth in the agency Strategic Plan for the 2021 through 2024 time period. These efforts were underway at the PSC well before the Performance Audit began and will continue long after the Audit. Ultimately, however, responsibility for enforcing Montana's ethics and disclosure statutes falls within the jurisdiction of the Montana Commissioner of Political Practices office, and not the PSC.

The Commission also concurs in that portion of the recommendation relating to Commissioner education and training. Again, the Commission recognized the benefit of such efforts well before receipt of the current performance Audit. To this end, the Commission has developed and implemented Commissioner and staff training related to quasi-judicial decision making and decision-making standards. Further, the Commission developed an enhanced new Commissioner orientation process. The orientation walks newly elected Commissioners through the duties and expectations of being a Commissioner, as well as educating the incoming commissioner on agency operations and the quasi-judicial process. Commissioners are slated to receive the State's ethics training course in the coming weeks and are encouraged to take administrative law online courses through the national judicial college.

What is more, during the 2023 legislative session, the Commission partnered with members of the legislature to develop an appropriations amendment for the very purpose of enhancing Commissioner ethics and performance training. The amendment, if passed, would have appropriated \$30,000.00 to the agency for Commissioner training purposes. See Amendments to HB 2, 2nd reading requested by Senator Dan Bartel. Ultimately, the amendment was never offered. The fact that the agency identified a need, such need is reinforced by the LAD, but the need was not funded demonstrates the Department's assertion that its management and operational success is dependent on the Legislature acting as its partner, not as an obstacle.

Again, The Department has completed 22 new internal policies to date and expects to have the final tranche completed in late spring of 2024, if not before. The final tranche will include a revised agency internal ethics policy.

RECOMMENDATION #2 (page 15):

Management and operational effectiveness.

The Department of Public Service Regulation should consider and revise the appropriate classification for management level positions.

Department response: Partially Concur.

Montana law makes clear the following. The Commission is the head of the PSC's Department of Public Service Regulation. The Commission is authorized, at its discretion, to hire six personal staff under an 'exempt' status. See, MCA 2-18-104. Ultimately, these exempt staff report to and answer to the Commission as the Department head. This is in keeping with other state agencies headed by elected officials, such as the State Auditor and the Secretary of State.

Further, by law, personal staff "serve at the pleasure of the agency head." See, MCA 2-18-104(5)(a). By their very nature, these positions are designed to be directly accountable to the five-member Commission for any misconduct or performance issues. Given that the Commission is ultimately responsible for the conduct of all PSC employees and accountable to the public for agency performance, the Commission does not take lightly any Audit recommendation that would remove staff accountability further away from the people of Montana.

As noted, in early 2021, under the guidance of new agency leadership, the Commission undertook an extensive review and survey of the agency, its operations, and its personnel structure. This effort, which was done with extensive employee input, resulted in both the adoption of a new organizational structure, as the same is set forth in administrative rule, and the adoption of correlating strategic planning organizational charts that better detail and define job responsibilities and chain of command.

These improvements resulted in tremendous improvement within the agency but are given only a cursory acknowledgment in the Audit Report. However, the strategic plan specifically details improvements to be made by:

- (1) enhancing fiscal performance of the agency's centralized services,
- (2) measuring agency performance and areas of risk annually,
- (2) increasing regulatory effectiveness by ensuring sufficient staffing levels and planning for loss of institutional knowledge due to retirements, and
- (3) conducting regular reviews of agency policies and rules to determine their current relevancy and effectiveness, among other improvements.

As stated, one major management structure change arising from that extensive internal review process was and is the creation of an executive director position. In substance, the position is designed to serve as the agency's chief of staff, assisting the Commission with management of the agency, but working under the direction of agency leadership, namely the direction of the Commission President and Vice President.

Contrary to what is asserted in the Audit Report, the new organizational structure provides extensive management authority to the executive director. This includes, again contrary to what the Audit Report represents, an active role in performance evaluations of all exempt and senior management positions. Based on this evaluation and performance review authority, the executive director also has the authority to recommend to the Commission President and the Vice President the need for discipline, termination, pay increases and/or other management actions. In fact, there are eight delineated major duties assigned to the executive director. These duties range from managing agency staff by balancing management staff workloads, to overseeing day-to-day general operation of the agency, to being primarily responsible for setting and monitoring the agency budget. Specifically, the eight duties include the following duties.

1. Plan, direct, manage, supervise, and coordinate the day-to-day administrative operations of the Department of Public Service Regulation.
2. Balance staff workloads and agency fiscal priorities to ensure wisest and best use of resources.
3. Manage department staff, including maintaining proper staffing levels, proficiencies, and schedules, and overseeing division administrators, supervisors, and support staff to ensure continual agency productivity, efficiency, and effectiveness.
4. Ensure the adopted plans, policies, and directives of the Commission are carried out and guard against all activities that are not consistent with the Commission's statutory authority or adopted plans, policies, or directives.
5. Oversee budget, appropriations, Audit compliance, legislative relations, and human resources matters of the agency.
6. Facilitate internal teamwork, communications, and orderly processes within and between employees, divisions, and Commissioners.
7. Prepare annual reports and make informational presentations.
8. Other duties related to the official business of the Commission as described in the position's job description or otherwise assigned by the Commission.

Indeed, the executive director is not given the authority to directly hire or fire appointed and management staff. Under the new agency structure, the five-member Commission retains that authority, which the Commission has always exercised. This helps ensure that all Commissioners have a say in hiring key personnel while, simultaneously, providing protections for exempt employees, since the processes of hiring or firing require a majority vote of the five Commissioners, as opposed to the unilateral decision of an unelected executive director.

What neither the executive director nor the Commission itself is tasked with is the day-to-day operation of the various divisions within the agency. That responsibility is delegated to the agency division heads. As a general matter, the division heads are granted broad authority and discretion to manage those divisions without extensive Commissioner oversight. It is the division heads that ultimately are responsible for managing and evaluating classified employees who work within their respective divisions.

With the creation of the executive director position, the division heads presently have a person clearly identified within the chain of command structure to whom they can report concerns relating to either Commissioner conduct or other management employee conduct; and they can do so without having to bring such concerns directly to the Commission President or Vice President. To this end, because the new agency structure actually brings greater accountability to all areas within the PSC, the Commission strongly disagrees with any assertion that the new agency structure is not effective and/or has created ambiguous lines of authority.

Turning now to the recommendation itself, during the course of the agency's extensive strategic planning work, the Commission contemplated how the exempt positions provided to the agency by the legislature should be allocated. Because the highest degree of accountability is inherent in exempt positions (which serve at the pleasure of the Commission as noted above), the Commission determined it would be prudent to keep with the past practice of maintaining exempt status for the top management positions within the agency.

As detailed by the LAD, one exception was recently made to remove the exempt designation from the agency's Chief Legal Counsel. This decision was made after careful review of agency needs, direction, and personnel. In accordance with the Audit recommendation, the Commission is open to

further consideration of the existing personal staff positions. However, after three years of work on the strategic plan, the Commission understands careful analysis of the pros and cons of designating which agency jobs should be filled with personal staff must be weighed carefully before making additional changes.

In closing, the Commission is open to further analysis regarding this Audit recommendation but has not yet been persuaded that implementing the Audit recommendation would be prudent. Further, in order to comply with this recommendation, it is important to keep in mind that the agency would be required to open the now exempt positions to the competitive hiring process associated with classified state positions, and current employees would have to reapply for their existing job and be rehired.

RECOMMENDATION #3 (page 21):

Management and operational effectiveness.

The Department of Public Service Regulation should address turnover and retention by proposing methods to the Legislature for funding the pay plan and increasing salaries for competitive positions.

Department response: Partially Concur.

The Commission agrees that providing competitive pay to its employees is vital to continued agency success. Further, the Commission concurs that staff turnover, particularly in the area of senior staff retirements, directly affects the Commission's regulatory mission.

As the executive director position is a newly created one within the agency, agency leadership is still evaluating the duties and expectations of the position to ensure that the position is effective for purposes of carrying out the agency's strategic plan. And as part of the continued agency management review process, the position will be evaluated with the Auditor's recommendation(s) in mind. Such review will be done, as prior agency management reviews have done, to have the least amount of management and staff needed to efficiently run the agency.

Since at least 2017, the Commission has made staff retention a priority. This is because during the 2017 Montana legislative session, the Legislature cut 3.5 FTE, thereby dropping the Commission to its lowest staffing level in almost two decades. At that time, prior Commission leadership warned the Legislature that this deep level of staff reduction would eventually result in workload issues, retention problems, and difficulty complying with state policies and legislative mandates. Time has borne these concerns out, particularly in the area of quality staffing in the PSC's centralized service, division where the required FTE reductions were realized.

In January of 2021, new Commission leadership faced a situation where staff was working from home due to COVID; there was strife among employee management; competency issues were clear and pronounced; the agency's case management software system was insufficient; and agency divisions were significantly understaffed. The last management issue was only compounded when the 2021 Montana Legislature eliminated an attorney FTE. Further, new agency management was working under budget and appropriations levels enacted by the 2019 legislature. Such levels were clearly problematically low when it came time for new leadership to redress existing deficient pay ranges for agency legal and centralized services, both as compared to the private sector and other state agencies.

As part of the 2021 comprehensive agency review, Commission leadership determined that there were several underperforming staff, as evidenced by the series of poor fiscal Audit results incurred by the

agency, and lack of metrics and measures to assess staff performance. In late 2021 through early 2022, underperforming staff were replaced with experienced state employees from other agencies. Though the positive results of these staffing moves have been significant, quality comes at a cost. The agency had to stretch its already tight budget to pay these employees at a level commensurate with their experience. Further, the agency made the difficult but correct decision to raise pay for its attorneys in order to retain these key employees and to dedicate resources to replacing and enhancing its public-facing case/regulatory filing system.

Difficulty in filling technical positions, such as those that are common at the PSC, is not unique to this agency. In October, the Legislative Audit Division provided a memorandum to the Legislative Audit Committee detailing the fact that, since July 1, 2019, financial compliance positions within that Division were vacant between 186 and 744 calendar days, with an average of 409 days. The LAD represented to this Committee that these positions were open for this lengthy time “despite repeated recruiting efforts.” The PSC understands the difficult position the LAD finds itself in when attempting to recruit and hire accountants and finds itself in the same position when attempting to hire attorneys, engineers, and economists – particularly at uncompetitive pay levels.

The tight budget constraints the Commission works under are exemplified by the fact that at fiscal year-end 2023, the PSC had approximately \$1,500.00 remaining in the personnel budget. The agency only ended the year in the black due to tough management decisions being made to keep two FTE positions unfilled for a significant time in order to achieve the legislatively mandated vacancy savings requirement. The agency was not immune to the ‘The Great Resignation’ or the ‘big quit’ period of 2021 and 2022, where employees across the country, including those working at the PSC, confronted their work–life balance. According to the Bureau of Labor Statistics, a total of 47 million Americans quit their jobs in 2021 alone. And it should be noted that the 5% annual vacancy savings mandate applies to all staff positions whether or not the position is filled for the entire fiscal year.

During the 2023 session, the agency requested the legislature authorize four additional FTEs for the agency in order to fill existing work needs and to redress existing staff workload concerns. The Legislature only funded two of those four position requests—one attorney and one IT analyst position. The Commission appreciates and values the addition of these valuable staff and thanks the Legislature for the authorization. Even so, the agency has an identified, real, and tangible, need for additional personnel – a need that presently remains unmet. Further, the agency requested that the burdensome vacancy saving requirement be lifted so that the PSC can fill both its external affairs and executive director positions, as the Auditors now recommend. That request was denied as well.

Again, the Commission cannot be faulted for legislative decisions, particularly when the agency has identified a need and requested legislative help with the same. This is why the Commission only partially concurs with Recommendation #3. As noted, the Commission has already identified insufficient position funding levels as problematic. It has also been identified that staff workload concerns can be addressed, in part, by adding additional FTE. The agency calculates that it will take an additional \$206,071.42 to bring all staff up to market rate. The PSC has no ability or authority to raise its own budget. Therefore, Recommendation #3 can only be implemented if the 2025 Legislature fully funds the agency’s proposed ‘methods’ for funding the state play plan and increasing position funding for competitive positions.

At the same time, the Commission also recognizes the 2023 Legislature enacted HB 13. This bill, which was signed into law by Governor Gianforte on April 11, 2023, increased the base salary of every state employee, including PSC employees, as of July 1, 2023, by \$1.50 an hour or 4%. State employees will receive a similar pay increase in July 2024. This legislatively imposed pay increase has helped supplement and bolster the agency’s already ongoing recruitment and retention efforts and the Legislature

should be recognized for enacting the same.

Further, as elected officials, Commissioners have a fiscal responsibility obligation to the public that funds government operations. To this end, the Commission's four-year strategic plan contemplates strategic and responsible pay increases for agency staff. However, these pay increases are to be primarily based on documented actual performance of the employee as well as market rate analytics. The plan recognizes that state employment comes with benefits not always afforded by those working in the private sector. The state benefits include paid holidays, annual leave, sick leave, health benefits, and retirement systems that not all private sector employers offer.

In short, agency leadership understands that one of the most common reasons for turnover at the DPSR is employees being recruited by or attracted to other government agencies who offer higher pay, more job flexibility, and more opportunities for advancement, factors that the PSC is currently cabined by due to agency size and budget.

Again, to comply with this recommendation, the Legislature would have to appropriate an estimated additional \$206,071.42 to bring all PSC staff to the midpoint of the 2022 Market Analysis.

CONCLUSION:

The Commission acknowledges the efforts of Audit staff during the two plus years it has undertaken this performance Audit. For those not involved in utility regulation, understanding the nature of the technical work performed at the PSC can be difficult. During the last three years, agency leadership has been balancing our highly technical, day-to-day work with implementing extensive reforms in all areas of agency operation in order to put the agency on its current path of operating as a model of good governance. The Commission appreciates the opportunity to comment on the Audit recommendations and will take the recommendations under further advisement for the year 2024 and beyond.

Regards,



James Brown, Esq.
President

On behalf of Vice President Jennifer Fielder, Commissioner Randy Pinocci, Commissioner Tony O'Donnell, and Commissioner Annie Bukacek.